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Business and Economic Conditions

New York, February, 1956

General Business Conditions

THE January business reports have again been good, except for the downward revision of automobile production schedules. Since the automotive industry is the largest buyer of materials, parts, and supplies in the country, even a modest curtailment causes some dampening of enthusiasm and takes something away from the force of the business advance. Together with the slippage in housing starts, which continued through December and has now lasted for some months, it signifies a narrowing and slowing of the rise, and possibly the reaching of the crest which so many have been expecting.

In other lines, however, there are few indications of slackening, and some are still gaining. Where a crest seems to be forming, as in steel and certain other industrial materials, it is due generally to limitations of capacity rather than to softening demand. In many industries, manufacturers would be producing more if they could possibly do so. Unfilled orders are heavy, often requiring capacity output for months to come. Incoming business holds at high levels. Machinery and equipment output and nonresidential construction are expanding. In the general merchandise trades, reports from the January wholesale markets, which reflect retail conditions and buyers' sentiments, have been uniformly good.

From all indications, the country will cross the invisible boundary line into a $400-billion-a-year economy, measured by the total output of goods and services, some time in the current quarter. There is no particular magic in this figure except as it emphasizes the rapid growth of the past year, the unprecedented height reached, and the way in which many lines must strain at the limits of manpower, materials, and capacity to make this possible. In the past year the extraordinary total of 3.1 million people have been added to the working force, and output of steel, nonferrous metals, glass, paper, and other materials has been pushed as close to capacity as is economically feasible. At such high levels, further gains are difficult and limited, while cutbacks in lines which have become temporarily overextended are to be expected. This is the situation in automobiles.

The stock market has been vacillating, and some tendency to shorten commitments is reported by purchasing agents. In view of the dangers of duplication of orders and excessive inventory build-up, which could only carry on the boom at the expense of later recession, conservative buying policies should be welcomed. None of these developments provides clear signs that business is at a turning point.

Prospects for Automobiles

The spotlight has focused on the automobile and homebuilding industries as primary sources of weakness in 1956. Both industries had remarkably good years in 1955, and both are currently operating considerably below their 1955

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highs. Harlow H. Curtice, president of General Motors, has predicted that domestic automobile production (excluding vehicles for export) will total 7.5 million cars and trucks in 1956, a decline of 14 per cent but still the second best year on record. The industry expects truck production approximately to equal the 1,050,000 turned out for domestic use in 1955; hence, the anticipated decline of roughly 1.2 million units from 1955 to 1956 would appear to be entirely in passenger car output.

The publicity given to cutbacks in auto output has tended to obscure the fact that retail sales of new cars are holding well up to last year's performance, which is no small achievement. In November, December, and the first 20 days of January, dealers sold somewhat more cars than they did a year earlier, when the new 1955 models were arousing so much interest. The key question is how long dealers can maintain this pace.

Whereas the '55 model year started off with low stocks and a moderate rate of production, output of '56 models quickly attained near-record levels and by December 31 had piled up dealers' stocks of 725,000 new cars, according to Ward's Reports. Since mid-December, manufacturers have been striving to bring production more closely into line with sales, but even so new car stocks at the end of January were probably at an all-time high. By eliminating overtime and Saturday work and by laying off over 25,000 workers, factories have cut passenger car output 23 per cent, from 178,400 in the week ended December 10 to 137,200 in the last week of January. For February, production is scheduled at about 600,000 cars, still a good rate for the off-season by pre-1955 standards.

The greatest part of the adjustment to date, by both auto manufacturers and suppliers, has been accomplished by a shift from overtime operations to a normal work week, which is hardly a depressed condition. Some suppliers, notably steel mills, have continued to operate at record levels because demand by other customers was so great. What little steel was released by auto companies has been eagerly snapped up. If dealers' new car sales start slipping, further production cutbacks are likely to follow, but to date the reductions in output and payrolls have not reached proportions that would fan out far into the rest of the economy; indeed, the release of materials may make it possible for some other industries to increase output. In any case, the restyled '57 models will provide a stimulus to the market in the latter part of the year.

The Housing Market

Home building has been declining for some time with little visible effect on over-all economic growth. The number of new homes started reached a peak seasonally adjusted annual rate of 1,478,000 in December 1954 and declined to 1,187,000 in December 1955. The cumulative effect of tighter mortgage credit, more restrictive terms, resistance to higher prices, and localized saturation of a few markets tended to accelerate the drop in the latter part of 1955.

More recently there have been indications that the tide is turning. The Home Loan Bank Board arranged in December to make as much as a billion dollars in stand-by credits available to Federal savings and loan associations. In January, the Veterans Association and Federal Housing Administration extended maximum maturities on mortgages guaranteed or insured by them from 25 to 30 years, reversing their action of last July. The Federal National Mortgage Association opened facilities for "warehousing" mortgages. Generally, funds available for investment in mortgages appear to be somewhat less tight. It is likely to be spring before it can be seen whether or not these changes are sufficient to halt or reverse the downtrend in housing starts. Meanwhile most experienced observers are reasonably optimistic. In both government and private building circles the consensus is that the number of units started in 1956 should reach or exceed 1,200,000, which is a little better than the December 1955 rate.

The number of dwellings started in December was down one-fifth from the peak a year earlier, but total expenditures on residential construction were off only 8 per cent from their 1955 high. The difference is attributable to rising construction costs, to demand for homes with more rooms and more special features, and to the rise in outlays for alterations and improvements. These trends will help maintain expenditures even in the face of a further decline in housing starts in 1956.

Offsetting Expansion

Whatever the contribution of the automobile and housing industries to economic activity in 1956, it is plain that the expected decline from the 1955 average level is already here to a considerable extent. In any case it is unlikely that autos and housing will carry the rest of the economy with them on the downturn in the same fashion that they sparked the general upturn in 1954-55. Substantial offsetting elements of strength are present in other durable goods and other types of construction, as well as in

the growth of consumer purchases of nondurable goods and services and the prospect for increased government expenditures.

The strength of these offsets is attested by contract awards for nonresidential construction, compiled by F. W. Dodge Corporation, which in the first three weeks of January were 39 per cent greater on a daily average basis than last January, and by new orders for machine tools, which came in twice as fast as shipments went out during the fourth quarter. Another example is the railroad equipment industry, which had on hand unfilled orders for ten times as many freight cars at the start of 1956 as a year earlier. These are typical of the markets for capital goods and the vigor of business investment plans.

Another likely source of support over the next few months is inventory accumulation. At the end of November, the book value of business inventories finally rose above the September 1953 peak of $81.2 billion, and they are doubtless higher now on a seasonally adjusted basis. Record-breaking stocks are only half the story, however. The economy is larger today than in 1953, and larger stocks are needed to keep it operating smoothly. Total business sales are up about 10 per cent since the fall of 1953 and gross national product nearly as much. With the outstanding exception of automobiles, there appears to be room for some further expansion of inventories without carrying stocks to speculative or dangerously excessive levels.

The rise in business stocks has been under way for approximately a year and with certain exceptions has been characterized by moderation and restraint. The hesitancy induced by growing doubts about the outlook will serve to keep buying policies from getting out of hand in the next few months. But two special forces are promoting accumulation of stocks at present. In textiles and several other industries, stocks are being built up in anticipation of higher prices after March 1, when the minimum wage will be raised by law from $.75 to $1.00. The rise is expected to boost directly the wages of about 2 million workers an average of 13 cents an hour, and through upward revision of the wage structure it will indirectly bring raises for many more. Steel mill customers have been reluctant to cut back deliveries, in order to build inventories against the possibility of a steel strike or price rise at mid-year.

Crosscurrents in Business

The foregoing summary signifies that the rise in the various parts of the economy is no longer uniform. Neither, however, is the leveling out or decline. Some sectors are expanding while a few contract. Some, like housing, may be nearing the end of their adjustment period. Others, like automobiles, are now in the adjustment process. Still others may have several months of sustained operations or even further gains ahead before a downturn occurs. A few may go through 1956 without the pains of adjustment.

In short, another "rolling readjustment" is under way. The net effect may be a gradual rise or a gradual decline, depending on the relative strength of the forces involved. In any case, simultaneous weakness in the major segments of industry and trade does not seem to be at hand or in sight.

In general, business confidence remains high. Actions speak louder than words. Within the past month the steel, automobile, and other important industries have announced plans for expansion and modernization running into billions of dollars. The managements of these large firms are willing to put huge sums into new plant and equipment in the expectation that there will be a prosperous and profitable economy in which to sell the goods these facilities will produce. In maintaining a high level of investment, they help sustain the prosperity they anticipate.

A Balanced Budget

President Eisenhower's annual budget message, presented to Congress January 16, projects a balance between federal revenues and expenditures for the fiscal year ended June 30, 1957. As a result of better-than-expected revenues, a balance is also struck for the current fiscal year ending June 30, 1956.

A balanced budget has become something of a museum piece in federal finance. Over the last twenty-five years revenues have covered expenditures only three times. The accomplishment caps three years of hard work finding ways to get the business of government done more efficiently and with an easier burden on the taxpayer. What turned the trick was growth in revenues, a product of prospering business.

Expenditure figures now show a tendency to move back up. Even if, as some expect, revenues surge beyond the Treasury forecast, little scope is provided for the much-debated election year tax cut. The President puts debt retirement ahead of tax reduction in this prosperous period but makes no real provision for either.

When the President became a candidate he set an objective of balancing the budget at a $60 billion a year level. The present prospect is for a balancing at $64 billion in fiscal '56 and

at $66 billion in fiscal '57. The revenue estimates assume that Congress will accept the President's recommendation that reductions in corporation income and excise tax rates, scheduled for April 1, be deferred for the third successive year. As the table shows, the estimate of revenues for the current fiscal year has been raised $4.5 billion since the original fiscal '56 budget was presented a year ago. Expenditures have been marked up $1.9 billion from the $62.4 billion originally projected.

(In Billions of Dollars)

	Fiscal '55 actual	—— Fiscal '56 Jan.'55 est.	Aug.'55 est.	Jan.'56 est. ——	Fiscal '57 Jan.'56 est.
Expenditures	$64.6	$62.4	$63.8	$64.3	$65.9
Receipts	60.4	60.0	62.1	64.5	66.3
Surplus(+) or def.(—)	—4.2	—2.4	—1.7	+0.2	+0.4

For fiscal '57 revenues are estimated $1.8 billion higher than this year, at $66.3 billion. An increase in outlays to $65.9 billion is proposed, leaving a token $400 million for debt retirement. The President explained:

> For years, many activities which are desirable for fostering sound economic growth have been postponed because of the overriding needs of war and defense.
>
> Defense needs are still overriding and must continue to be met in full measure. However, budget revenues now permit us to undertake some new and expanded programs for enhancing opportunities for human well-being and economic growth. This budget reflects that purpose.

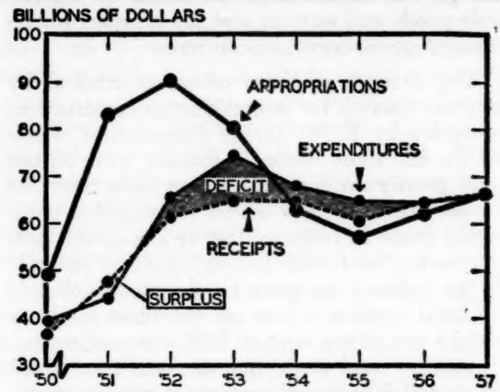
This line of thought, and the upturn in programmed expenditures, stand in contrast to the philosophy of earlier budget messages. In presenting the fiscal '56 budget the President had stated:

> The growing strength of the United States and its friends is a key factor in the improved outlook for peace. We must continue to build this strength. We must at the same time preserve our liberty at home by fostering the traditional initiative of the American people.
>
> We will increase the scope of private activity by continuing to take Government out of those things which the people can do better for themselves, and by undertaking on a partnership basis, wherever possible, those things for which Government action is necessary. Thus, people will be able to keep more of their earnings to use as they wish.

It looks as though the public spending lobbies have forced a change in the basic line of administration economic philosophy.

Expenditure Upturn

Moderate increases in expenditures are distributed pretty much throughout the fiscal '57 budget, as the second table shows. The increase for National Security is attributed largely to rising costs of the complex technology of modern war — air-atomic power, guided missiles, continental defense and the latest types of troop



U.S. Government Net Receipts, Expenditures, Deficits, and Appropriations (New Obligational Authority) by Fiscal Years, Figures for 1956 and 1957 Estimated.

weapons. The foreign military aid portion is increased slightly to $2.5 billion.

U. S. Government Expenditures by Major Programs Fiscal Year 1957

(In Millions of Dollars)

	1957 Estimated	Amount above or below 1956 Estimated	1955 Actual
National Security	$40,370	+903	—256
Int'l Affairs and Finance	2,108	+ 55	— 78
Veterans' Benefits	4,879	+ 86	+422
Labor and Welfare	2,995	+228	+443
Agriculture	3,364	— 12	—1,047
Natural Resources	1,031	— 14	— 50
Commerce and Housing	2,071	—111	+449
General Government	1,757	+146	+556
Interest	7,066	+191	+628
Reserve for contingencies	225	+125	+225
Total	$65,865	+1,595	+1,295

Also up from fiscal '56 is projected spending on International Affairs and Finance, most of which reflects foreign economic aid. These two categories account for $958 million of the total $1,595 million increase in spending over the fiscal '56 level. The remaining $637 million would go to expand civilian programs which, in the words of President Eisenhower:

> are designed to build for the future by assisting further in the strengthening of agriculture; in the promoting of labor standards; in the building of schools; in the expansion of research and training in science, health, and agriculture; in the modernization of our highways; in the improvement of housing and urban facilities; in the enlargement of our airway traffic capacity; in the replacement of our merchant fleet; and in the conservation of our natural resources.

Some doubts have been expressed as to whether expenditures may not be seriously underestimated as were the initial estimates for fiscal '56. Congressmen have already expressed opposition to the President's plan to finance the new farm program in part out of sales of existing CCC surpluses. Thus the $1 billion drop from the fiscal '55 cost of agricultural programs hangs in doubt. The President allowed a record

$844 million for federal aids to the States under existing highway programs but made no provision for the new ten-year Federal-State Interstate Highway System beyond suggesting that it should be "soundly financed so as not to create budget deficits." He counts on a $350 million raise in postal rates to reduce the post office deficit – and to offset increases in other items under the heading of Commerce and Housing. Whether the Congress will go along, after refusing to do so last year, remains to be seen.

These considerations dampen hopes that under-estimation of fiscal '56 and '57 revenues may leave sizable surpluses for tax reductions.

Federal Aid for Schools

The increase from fiscal '56 under the heading of Labor and Welfare, second only to the rise in national security spending, is explained mostly by the initial $150 million cost of a proposed $1¼ billion five-year program of federal grants-in-aid to help the States meet general school construction needs.

As the President stated in his message on education sent to Congress on January 12:

> The responsibility for public education rests with the States and the local communities. Federal action which infringes upon this principle is alien to our system. But our history has demonstrated that the Federal Government, in the interest of the whole people, can and should help with certain problems of nation-wide scope and concern when States and communities – acting independently – cannot solve the full problem or solve it rapidly enough.

The grants-in-aid are designed as an emergency expedient to help the States catch up on school building. A federal agency in Washington would distribute the money according to a judgment of "need" and of effort being applied locally.

Proposals are already before Congress calling for a commitment of $400 million a year for four years; as much as $1 billion a year has been mentioned. The States and local governments are now spending more than $2 billion a year for school building and, in all, about $9 billion a year for public schools. There is no question but that aids to public education, once federal responsibility is asserted, could make some heavy demands on the federal budget. Before venturing down the path it would be wise to consider the basic principles.

Every day citizens are meeting with school boards to thrash out problems of school building, staffing, and curricula, weighing cost against need and preparing projects for the voters' decision. Within their means, people are willing to pay taxes for education as they have been doing since the nation was born. They naturally want better education for their children. But they also want to keep control of that education close to home, where they can keep an eye on it. Every previous campaign for generalized federal aid to education has foundered on the American people's instinctive fear that centralized financing will lead to centralized and distant control of what their children would be permitted to learn. Such control strikes at the citadel of American democracy.

Luther A. Weigle, Dean Emeritus of the Yale Divinity School, has stated that:

> It is not possible to distribute federal funds for education without the imposition of an increasing measure of Federal control in matters of educational policy. Federal control of education, at any level, would be calamitous.

Many people share the suspicion of Roger A. Freeman, assistant to Governor Langlie of Washington and consultant on educational finance to the Committee for the White House Conference on Education, that the Congress is being panicked into federal control of education by propaganda. Writing on "Federal Aid to Education – Boon or Bane?" last fall he asserted that: "The present rate of school building construction is more than sufficient to take care of the enrollment increase." The real problem of school financing, he said, is the high rate of federal taxation which drains away local resources:

> All major tax sources are available to the states. But the federal government has just about exhausted the willingness of the American people to be taxed. The only effective restriction upon the fiscal powers of the states is the size of the federal tax burden. This restriction can be eased by reducing the financial commitments of the federal government, and not by adding to them.

Other Programs

The school program is only the most controversial of the new or enlarged spending projects. The fiscal '57 budget shifts the emphasis of budgetary policy quite generally from reducing and eliminating federal spending programs to the expansion of existing programs and the establishment of new ones.

There is not space in these pages to discuss the numerous new programs that the President's messages endorse in the areas of agriculture, education, highways, research, and aids to labor surplus areas. The amount of money involved usually is modest – indeed only a drop in the bucket in many cases compared to what individuals, industry, State and local governments, private agencies and foundations are spending. Yet it adds up. And each new program, however modest at the outset, becomes a nucleus of pressure for bigger demands in future years.

It is not that the projects may not be good and useful. The waste lies in useless duplications of effort and the sprawling of wasteful bureaucracies into every area of human activity.

It would be a good thing if the choice between bigger federal spending and lower federal taxes could emerge as a clear issue in the election this fall. The results of last November's state and local elections throughout the country showed the American people exercising careful and wise discrimination among spending projects and keeping a weather eye on public debt and tax burdens.

Fiscal Policy at the Crossroads

In concluding his budget message the President alluded with pardonable pride to the prospective achievement of a balanced budget after the $7.4 billion of tax reductions made effective in 1954. As he stated:

> This course of Government policy has helped to lay a sound basis for the greatest volume of business, the highest employment, and the highest national income in the history of this country.
>
> As an essential element in this prosperity, private spending has more than replaced reductions in Federal spending. Federal expenditures have declined from 20.6 per cent of total national production in the fiscal year 1953 to 17.3 per cent in 1955. This budget is designed to continue that trend.
>
> We have freed the economy from needless controls and from inflationary deficits, and have reduced the tax burdens which threatened to destroy the incentives to work and save and invest. State and local governments are now in an excellent position to obtain revenues and meet their responsibilities.

The project of balancing the budget *and* reducing taxes was bold and imaginative at its outset. The plan demanded a radical contraction in federal expenditures from $77.9 billion programmed by the preceding Administration for fiscal '54. The $64.3 billion figure for fiscal '56 is $13.6 billion lower. It demanded a negotiation of a cease-fire in Korea. This was accomplished. It assumed that tax cuts would energize private enterprise and spending. By the natural response of people to opportunity, the President's faith was redeemed. At lowered tax rates the revenues are now surging up to and beyond the $64.8 billion collected in fiscal '53, before the tax cuts.

Speaking by television to the "Salute to Eisenhower" dinners on January 20, the President coupled a review of the achievement with the warning: "We must not relax merely because the general record is good." Yet the budget is one that loosens the rein on public expenditure. *The Economist* of London, reviewing the U.S. budget proposals, bluntly asserts: "The days of declining spending by the federal government are over . . . This is big government with a vengeance: it is welfare state and more besides."

What *The Economist* seems to imply is that—as in the experience of Great Britain, reputedly the most heavily taxed nation on earth—bureaucracies won the battle over the taxpayer and will hold their mastery. A leading British industrialist, Sir Bernard Docker, now is leading a campaign for a 1 per cent cut in government spending. On January 26 he stated:

> What I am doing is to call on every voter in this country to pelt the politicians with postcards and petitions till their trembling knees become stiffened enough, with your backing, to allow them to stand up for our rights.

What Sir Bernard has in mind is the direction of public spending policy. We ourselves have had some costly experiences trying to build stable progress on a foundation of rising public expenditures.

The budget was balanced in 1930 at a $3.4 billion level of federal expenditures with a 100-cent dollar.

It was balanced next in 1947 at a $39.0 billion expenditure level with a 75-cent dollar.

It was balanced the last time in 1951 at a $44.1 billion expenditure level with a 64-cent dollar.

Now the prospect is for a balance at a $64 billion expenditure level with a 62-cent dollar.

If the Congress accepts and enlarges upon the proposal to increase federal expenditures, no one can say how much less the dollar will be worth before a balance is struck again.

A Critical Choice

The Congress has a critical choice:

1. Discard the idea of a balanced budget in order to spend more.

2. Use substantially all the revenues, on the pattern of the President's budget, to help States and local governments build schools and roads and generally enlarge federal spending programs.

3. Control expenditures to develop surpluses for debt retirement. The federal debt on December 31 was at a peak, within $1 billion of the $281 billion public debt limit and $18 billion higher than at the close of World War II in August 1945. We had the debt down to $255 billion at the outbreak of the war in Korea.

4. Control expenditures to reduce taxes. The personal income tax exemption of $600 is $100 higher than during World War II; the excess

profits tax is gone; and tax regulations are generally easier. But the corporate tax rate is 52 per cent against 40 per cent during World War II. Personal tax rates are within a stone's throw of the peaks of World War II; actually they are higher if account is taken of the shrunken value of the dollar. A federal sales or excise tax affords the only taxing power left for an emergency.

Give Up a Balanced Budget?

The first alternative is frankly to give up the idea of a balanced budget. It has become a little old-fashioned to talk about a balanced budget. At hearings conducted in December by the Mills Subcommittee on Tax Policy of the Congressional Joint Economic Committee the main stress was laid on needs to spend more money or to reduce taxes, without particular reference to the balance of the budget. The report of the subcommittee, dated January 5, addresses attention to "the balanced growth of the economy" and makes no direct reference to the balance of the budget.

On the other hand, the President and his fiscal advisers have laid great and proper emphasis on fiscal integrity and the balanced budget principle. The Congress, accepting the leadership of Senator Byrd, has made the public debt limit a symbol of resistance to deficit-financing. A balanced budget is one clear sign that things are under control. An unbalanced budget is a warning to expect rising prices, threats of price controls, political attacks on merchants and manufacturers for profiteering, and recommendations of higher taxes for everyone.

There is or was a theory, applied by President Roosevelt during the Great Depression, that increased government outlays would stimulate business and hence the revenues and balance the budget. The theory did not work. There was a feverish, and incomplete, recovery followed in late 1937 by one of the sharpest drops in business in our history.

Professor Alvin Hansen of Harvard is one of those who held that Mr. Roosevelt's experiments failed because government expenditures were never increased enough. In 1952 he suggested that we had "an Alice in Wonderland economy" in which the more the government spent and the higher taxes went the more we had left for investment and spending. The voters in the national election that year rejected this prescription of an endlessly rising public debt and endlessly shrinking dollar. Too many people had learned, as Alice did from the Red Queen, that it took all the running they could do to keep in the same place.

Spend to the Hilt

Should the Congress choose the second alternative, and determine to spend every dollar of revenue, it would remove any possibility of debt retirement and destroy both the hope of tax reduction and the optimism and forward-planning based on the hope. It would involve a negation of the principles (a) that fiscal policy should be directed toward compensating fluctuations in the private economy and (b) that taxes should be patterned to encourage people to work harder to get ahead in life.

We aspire these days to maintain a top level of production and employment without inflation. When the private economy surges ahead, and incomes rise, people have to turn over higher percentages of their total incomes to the Federal Government. If expenditures are held back, surplus revenues subtract money from the spending stream and help resist tendencies of prices to be driven up by excessive demands on the markets.

It is demanding a good deal to expect Congress to spend less when revenues are flush and everybody else is spending more. Yet the economy needs this balancing force.

There are some who honestly doubt the capacity of the private economy to stand a drain of surplus revenues for debt retirement. If this view is correct, we have all the more reason to restrain expenditures and give tax relief. There is a limit of tolerance on tax-paying capacity within a stable and well-ordered economy. The narcotic of rising government expenditures and price inflation can raise the limit for a time, with the natural aftereffects of collapse. The "needs" for bigger and better federal spending programs must be reckoned against this potential cost.

The Public Debt

In war the federal debt rises under the weight of swollen expenditures. In a business slump it rises under the influence of falling revenues. The only time we can reduce the debt is in years of peacetime prosperity. As of this moment we have not paid off one dollar of the debt incurred in the minor Korean War to say nothing of the heritage of debt from the Great Depression and World War II. When the fiscal '57 budget was being presented the debt was pressing close against its $281 billion limit and Treasury cash balances were at a level equivalent to no more than two weeks' outlays.

This is the financial position of a Government eagerly looking around for new ways to spend money, pondering more financial aids to state

and local governments as though the financial position of the Federal Government were better than that of the smaller political units.

The failure of the Government to develop out of prosperity revenues for debt retirement is not due to any shortcomings of tax rates, most certainly not so far as income taxation is concerned. A general sales or excise tax might bring in money for debt retirement but the wiser solution would be to chisel expenditure programs and resist temptations to launch new programs regardless of the availability of funds, the desirability of debt retirement, and the needs that will arise for stimulating work and production by income tax reliefs.

Tax Cuts

The President's Economic Report, transmitted to Congress January 24, impliedly favors tax reduction if the economy stands in need of stimulation but otherwise urges application of any surplus revenues to "reducing our huge public debt":

> Such an act of fiscal integrity would signify with unmistakable clarity that our democracy is capable of self-discipline.

The innumerable recommendations for increased public spending, modest as they are by some past standards, raise the question whether the battle for self-discipline has not already been lost to the powerful lobbies that promote bigger federal spending at the expense of the taxpayer.

Tax reduction has a hard row to hoe. Opposition comes from both ends of the political spectrum – from conservatives who urge priority for debt retirement and from neo-liberals who distrust the ability of the individual to choose wisely how to spend his money and wish to have a federal officeholder spend it for him. On the other hand, advocates of tax reduction and debt retirement join in their concern over the level of public expenditure. As a matter of fact, if public expenditures are held down taxes and the debt can come down together.

Pruning expenditures and tax rates may be the only way to stop the rising drift of the public debt. The fiscal '57 budget, narrowly balanced as it is, is a point of unstable equilibrium in the sense that a removal of hopes of tax reduction can spill the economy into a slump and the budget back into a deficit position. Holding down on expenditures, and encouraging people by income tax rate reliefs to earn taxable income, is the most promising route to debt retirement as it is to generating efforts and productive investments for progress.

Today we have an optimistic, forward-looking economy projecting ambitious plans years into the future. An essential ingredient in the optimism has been the expectation of easier taxes in the years ahead. This ingredient removed, the dish loses flavor. People turn their efforts from producing taxable income to avoiding taxation and finding hedges against chronic inflation.

Throughout history the greatest single cause of inflation has been high and rising government spending. Neither inflation nor extravagant taxation has ever been the road to stable progress. The sound course is to restrain public expenditure, building surplus revenues so that a tax cut can be applied when needed within a balanced budget.

President Eisenhower in 1953 applied a plan that worked. It should be repeated.

Automation and the Labor Force

During the postwar decade, this nation has made vast strides in technology, particularly in the field of electronics. The fruits from years of research and development are finding rapidly increasing application in factories and offices. The spectacular performances of automatically controlled assembly lines and complex electronic computers have captured the popular imagination, but they have also aroused concern over the impact of this "automation" on employment.

Worrying over "technological unemployment" is, as we know, an old story. It has been characteristic of periods of economic recession, when factory layoffs caused by decline in demand have raised the old cry of "machines putting people out of work". The recession year 1954 was no exception, and as late as the spring of '55 people were still talking about the "failure" of employment to keep pace with rising industrial output. One manifestation of this concern was the announcement last July of a Congressional inquiry into the impact of automation, to be conducted during the fall by a subcommittee of the Joint Economic Committee headed by Representative Wright Patman of Texas.

Actually, by the time of the subcommittee hearings in October, the business boom and the rise in employment to new record heights had put a damper on the more extreme talk regarding the effects of automation. But this did not settle the question. As brought out in the hearings, there are wide differences of opinion among business men, government officials, and labor leaders as to the potentialities of automation and on how the gains therefrom should be divided. While the testimony helped to dispel

some of the old fears, it created new misgivings, especially — as the New York Journal of Commerce put it — with regard to organized labor's assertion of prior claims to productivity gains, the actual or even approximate dimensions of which are not predictable.

The report of the subcommittee itself, rendered late in November, is marked by commendable restraint. It takes a middle-of-the-road course, subscribing neither to a doctrine of complacency nor to threats of disaster. Recommending careful study and not precipitate action, it wisely concludes that "no specific broad-gage economic legislation appears to be called for" at this time as a result of technological changes.

What Is Automation?

The word "automation" is, as the report pointed out, so new that it is not found in most dictionaries. Yet it has widespread usage today, not merely in trade journals, but also in popular newspapers and magazines. Many people use it to embrace all types of mechanization and technological development, while others prefer a more specialized meaning.

Over the years, mechanization has been replacing human power with machine power. Automation proceeds one stage further and replaces human control of production processes with automatic control. Integral parts of automation are automatic "feedback" controls, which allow a machine to regulate itself and to adjust its performance to predetermined quality standards, and materials handling devices which transfer work from one machine to the next "untouched by human hands".

No witness at the Congressional hearings opposed automation or advancing technology as such. Few Americans in this day and age want to put themselves on record as opposing progress. Even Walter Reuther, vice president of the AFL-CIO, who has beaten the alarm drums over automation as much as anyone, acknowledged some benefits (albeit not without conjuring up the usual bugaboos) when testifying before the Joint Economic Committee a year ago:

> Automation holds out the promise of vast improvements in living conditions, leisure, and national strength. It likewise promises the elimination of routine, repetitive jobs. But the widespread introduction of automation within the coming decade or two will present us with serious economic and social problems, involving dislocations of the labor force, geographical shifts of industry, labor displacement, the upgrading of labor, and the need for substantial yearly increases in consumer purchasing power for rapidly growing markets.

Impact of Automation

Many people, hearing of marvelous new machines, are fearful that automation will reduce the amount of labor needed and thereby jeopardize jobs. In certain cases, as brought out in the subcommittee report and in the hearings, it will. The problem of adjusting to technological change is a human as well as an economic one, and some workers, particularly the older and more settled ones, will encounter difficulties in shifting to new jobs. That has been the case for the last hundred and fifty years or more, but it is a proven fact also that in the long run technological progress creates more jobs than it destroys.

The problems stressed and the solutions advanced in much of the unions' testimony lead to the suspicion that to some extent "automation" is just another peg on which to hang recurring demands for higher wages, guaranteed pay, shorter hours, increased social benefits, more public works and government intervention in the markets. All this is in advance of any real knowledge of the magnitude of productivity gains likely to flow from the new machines and methods.

The report addresses a timely admonition to organized labor regarding distribution of the benefits of automation which is of interest also to the great body of consumers outside the organized labor ranks. Referring to frequently expressed hopes that the fruits of automation may permit further reduction in the workweek from 40 to 35, 32, or 30 hours, the report calls attention to the choice between added leisure and added products and comforts, and goes on to say:

> As a society, we shall have to give thought to making sure that the gains of productivity and the shortening of the workweek are sufficiently generalized so that those in trades and places remotely removed from automated manufacturing lines may come in due time to share in gains whatever the choice may be . . . We do still have in this country substantial groups of comparatively underprivileged and lower income groups who should be remembered before those in the more favored industries can conscientiously turn to a shortened workday or longer weekend.

The two basic problems in assessing the impact of automation are how widely and how rapidly it is likely to be applied, and how much it will increase productivity and directly decrease the need for workers. Expert testimony at the hearings indicates that the impact will probably be less than popularly imagined, though precise forecasting is difficult in a field where human inventiveness and ingenuity play so large a part.

The factory of tomorrow is often pictured as a maze of complicated machinery, a few pushbuttons, and hardly any workers. Actually, as stressed in the hearings, a great many industrial processes and still more nonmanufacturing operations cannot use automation profitably, and

are unlikely to do so because of lack of standardization of products, need for personal services, space requirements, or cost of equipment. Construction, agriculture, mining, retailing, services, and the professions fall largely into this category. In other lines only partial application of automation is possible.

One expert, Walter S. Buckingham, Jr., of the Georgia Institute of Technology, has estimated that "automation will probably be limited to industries which employ at the most 25 per cent of the labor force." Even with full automation these industries would still retain a large proportion of their workers. The subcommittee's report finds that "increasing numbers of workers will feel the impact of automation", but that "it is important to note that not all workers, indeed only a relatively small, although conspicuous, fraction of the total labor force will be directly involved."

Changes Not Overnight

Moreover, industries cannot convert to automation overnight. One authoritative appraisal indicates that even the small group of industries "ripe for automation" in the near future will not displace more than half their workers over the next twenty years. In the war and postwar periods the economy has successfully weathered far larger shifts in employment in a far shorter span of time. Compared with the normal rate of turnover in the labor force — voluntary quits alone amounting to 2 per cent of factory employment each month in good times — the relocation problems raised by automation are by no means unsurmountable.

Aiding in the transition will be the tendency for technological progress to increase over-all employment at the same time that it displaces specific workers. Automation is used to cut costs and improve quality. A better, cheaper product then leads to increased demand and consequent stepping up of production and employment.

Although automation may displace direct labor in a given factory, it tends, as the subcommittee report points out, to increase the need for maintenance and engineering employees. It has given rise to whole new industries to supply and service automation equipment; from virtually nothing in the early postwar period, production and sales of automation equipment grew to a $3 billion industry in 1954, and by 1960 it is estimated that sales will reach $10 billion.

It has made possible entirely new products and greatly improved goods and services of a more familiar kind as well. The report states: "Perhaps the most conspicuous case involves atomic energy and atomic isotope technologies. In these cases, the very nature of the materials to be dealt with are such that they could never have been harnessed by hand methods and close human contact."

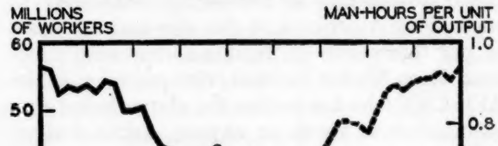
As automation speeds the output of autos, television, and other goods, it stimulates the growth of countless local enterprises devoted to servicing and repairing these products.

Evidence on Productivity

Individual automatic machines have produced dramatic increases in output per man-hour, but when combined in an average for the entire firm, or industry, the results are less striking. For manufacturing as a whole, recent years do not appear to have brought such sharp advances in productivity as would threaten employment opportunities. In fact — so far as productivity statistics can be trusted — the advances since the war represent merely an extension of a long-term trend.

Thus, in the period 1947-53 the annual increase in output per man-hour in manufacturing, according to data compiled by the U.S. Bureau of Labor Statistics and embodied in Secretary of Labor Mitchell's testimony before the subcommittee, averaged between 3.0 and 3.6 per cent. This is substantially less than the rate of increase in the comparable time period after World War I (about 5 per cent) and roughly in line with the long-run increase from 1909 to 1939 (3.3 per cent).

Nor do tentative data for 1954 and '55 indicate any significant acceleration of productivity gains compared with the earlier postwar period.



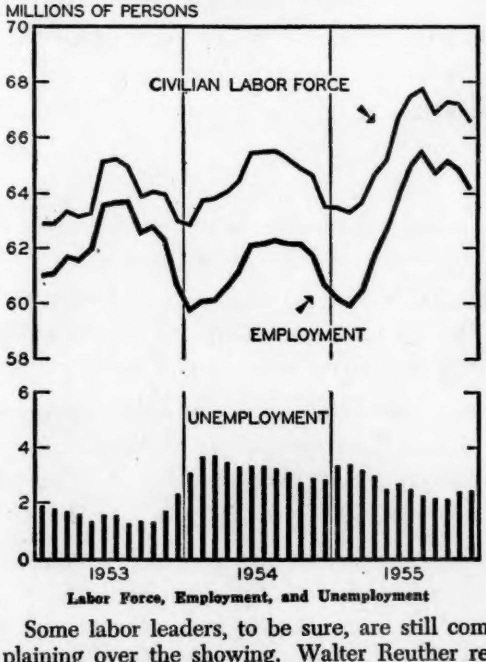
Employment and Labor Requirements in Private Industry, 1910-55 Based primarily on data from the Joint Committee on the Economic Report. Employment excludes government service.

The truth is that history affords little support for the idea, apparently held in some labor circles, that an expanding labor force and increasing productivity constitute threats to prosperity. To a business man, productivity (or output per man-hour) is more meaningfully expressed in reverse as labor requirements per unit (man-hours per unit of output). As shown by the chart on the preceding page, the average amount of labor required per unit in the private economy today is only half what it was 20 years ago, and two-fifths what it was in 1910.

Yet the over-all need for workers has not declined, but has increased with the demand for more and more output, and is now greater than ever.

The Booming Job Market

Meantime, while all this theorizing about machines and jobs has been going on, the unemployment situation itself has been rapidly clearing up. As shown by the next chart, based on Census Bureau reports, employment at the year-end totalling over 64 million jobholders was the highest for any December on record, while unemployment estimated at 2.4 million was the lowest for any December since 1952.



Labor Force, Employment, and Unemployment

Some labor leaders, to be sure, are still complaining over the showing. Walter Reuther recently noted among bearish factors in the economy "the persistence of a relatively high level of unemployment"; and George Meany, president of the AFL-CIO, in a year-end statement warned against complacency about the present economic plateau "while 3½ per cent of the nation's workers are still unemployed."

A look at the chart should, however, dispose of such complaints. It will be seen that at the 1955 seasonal peak during the summer, employment approximately equaled the total labor force of only a year earlier. Over the year employment rose by an amount approximately equal to the reported unemployment, a great many of these jobs being taken by new increments to the labor force — many of them women and teen-agers, often on a part-time basis — attracted in exceptionally large numbers by high wages and other inducements offered by employers hard pressed for help.

At the same time, unemployment among family heads and other steady members of the labor force dropped sharply, as did the number of long-term unemployed. Dozens of localized pockets of unemployed disappeared.

What happened last year was evidence of prosperity — over-employment and not under-employment. At about 3½ per cent of the labor force, unemployment is generally agreed to be close to minimum frictional levels. In many areas it is getting more and more difficult to find workers with certain skills. One of the blind spots of the unemployment data is the lack of information on how many job openings there are, since unfilled job opportunities are not counted.

Heart of the Problem

When business activity and total employment are at high levels the problems of adjusting to automation are minimized and localized. A booming job market greatly eases the relocation of workers. This was the heart of the subcommittee's report:

> The best and by far the most important single recommendation which the subcommittee can give is that the private and public sectors of the Nation do everything possible to assure the maintenance of a good, healthy, dynamic, and prospering economy, so that those who lose out at one place as a consequence of progressive technology will have no difficulty in finding a demand for their services elsewhere in the economy.

We have a "good, healthy, dynamic, and prospering economy" now. To attempt in this generally tight situation of full-capacity operations to deal with the last vestiges of unemployment by over-all stimulants would be highly dangerous. It would invite serious inflationary strain, leading ultimately to deflation and an unemployment situation that would really be something to worry about.

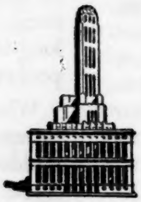
HIGHLIGHTS of 1955

from the Annual Report of

The First National City Bank of New York

and

City Bank Farmers Trust Company



On March 30, 1955, The First National Bank of the City of New York was merged into The National City Bank of New York, and the name was changed to The First National City Bank of New York. The merger increased our deposits and earning assets, and brought us new customer relationships, new personnel, and a greater potential for growth.

In 1955:

▶Total resources of the Bank increased to $7,001,000,000 and deposits to $6,309,000,000.

▶Operating earnings, after taxes, totaled $42,-466,976 ($4.25 per share on 10,000,000 shares outstanding).

▶Operating earnings less losses on sales of securities totaled $40,287,444 ($4.03 per share).

▶Dividends paid totaled $24,500,000 equal to $2.45 per share. Quarterly payment of 65 cents on November 1 was at an annual rate of $2.60.

▶Total salaries paid here and abroad came to $57,233,000. Taxes and assessments accrued totaled $41,666,000, before the credit for the transfer to the "Bad Debt" reserve.

▶Capital funds at the year-end total $592,446,606 ($59.24 per share) compared with $584,700,-224 ($58.47 per share) a year earlier.

▶Four new overseas branches (three in the Middle East), one overseas affiliate and one military facility were established. Two new domestic offices were opened.

▶The Bank has at the year-end 73 domestic branch offices and 66 overseas branches, offices and affiliates. Depositors number 1,065,000, staff 15,338 and shareholders 64,987.

For copy of complete Annual Report, write the Public Relations Department, The First National City Bank of New York, 55 Wall Street, New York 15, New York.

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